

# **CAPITAL PROJECTS AND BOND OVERSIGHT COMMITTEE**

## **Minutes**

**July 15, 2003**

The Capital Projects and Bond Oversight Committee met on Tuesday, July 15, 2003, at 1:00 PM, in Room 129 of the Capitol Annex. Senator Robert Leeper called the meeting to order, and the secretary called the roll.

Present were:

Members: Senator Robert Leeper, Co-Chair; Senators Tom Buford and Jerry Rhoads; Representatives Robert Damron and Paul Marcotte.

Guests testifying before the committee: William Pennell, Kentucky State University; Aldona Valicenti and Terry Thompson, Governor's Office for Technology; Bill Hintze, Governor's Office for Policy and Management; Armond Russ, Finance and Administration Cabinet; Warren Nash, Economic Development Cabinet; George Burgess and Tom Howard, Office of Financial Management; and John Nicholson, Kentucky Horse Park.

LRC Staff: Mary Lynn Collins, Pat Ingram, Nancy Osborne, Kevin Mason, Ben Brammer, and Shawn Bowen.

Senator Buford made a motion to approve the minutes of the June 17, 2003, meeting as submitted. The motion was seconded by Senator Rhoads and passed by voice vote.

Senator Leeper called on Ms. Collins to review correspondence and information items. Ms. Collins said included in members' folders was correspondence from Bill Hintze, Deputy State Budget Director, Governor's Office for Policy and Management, in response to a question raised at the June committee meeting regarding replacement firearms for the Kentucky State Police; quarterly construction reports from the Administrative Office of the Courts, the Finance and Administration Cabinet, and those universities that manage their own construction; and the Kentucky Lottery Corporation's monthly financial report for May 2003. Ms. Collins said also included in members' folders was the monthly staff update on various capital projects.

Senator Leeper asked if the purchase of the firearms for the State Police is now on a fast track. Bill Hintze, Deputy Budget Director, indicated it was.

Representative Marcotte noted that the staff update in the folders indicated a roof for the Kentucky International Convention Center was being replaced. He asked about the age of the roof. Mr. Hintze said the older portion of the convention center, on which the roof is being replaced, was built in the 1970s.

Senator Leeper said last month the committee reviewed an unbudgeted project submitted by the Finance Cabinet on behalf of Kentucky State University (KSU). The project involved the purchase of a new IBM mainframe, to be financed by IBM. While the committee approved that request, a question arose as to whether the best financing option available to the university was vendor financing. Senator Leeper said Mr. William Pennell, KSU's Chief Financial Officer, has returned to the committee today to report on a modified financing plan.

Mr. Pennell said the university investigated other financing options including GE Capital since the state has negotiated a master lease agreement with that company. He said they have now concluded that the GE Capital Lease is the best option, and they plan to use GE Capital to finance the new equipment.

Senator Leeper said last month the committee reviewed several information technology project requests, and based upon that review, a number of issues were raised concerning financing of technology projects and what to do when vendors withdraw support from existing technology systems. As a result, he said the committee invited the state's Chief Information Officer, Aldona Valicenti, to attend the day's meeting to discuss the state's strategy to address information technology needs and procurement.

Ms. Valicenti said vendor support can be divided into three areas – hardware, software, and application. She said computer hardware has a useful life of three or four years; anything past that time period probably has exceeded the warranty of that hardware. Ms. Valicenti said the hardware associated with mainframe computers can be extended beyond its useful life with additional enhancements from the vendor or doing hardware upgrades in stages.

Ms. Valicenti said when a vendor withdraws support for hardware that has been in the marketplace for a long period of time, the vendor will normally inform the customer that they feel the hardware is no longer useful. Formal notification of hardware obsolescence usually comes from the vendor 18 or 24 months before support is to be terminated. She said in the case of the IBM mainframe at KSU, IBM formally announced in February 2002, they were discontinuing the hardware. She said the vendor normally provides enough lead time for an agency to look for alternate hardware or find different ways of running that processing.

Ms. Valicenti said the utility software and application software follows a similar path as the hardware. The vendor will signal early on when they plan to upgrade

software. She said it is prudent for the customer to be in sync with the upgrade package since an upgrade provides better processing and new capabilities. Ms. Valicenti said it is most important for an agency to make sure there is appropriate maintenance support, whether it is under warranty or a specific arrangement.

Mr. Terry Thompson, Executive Director of Administrative Services, Governor's Office for Technology (GOT), said GOT is required to follow KRS Chapter 45A for financing any projects. Since the state has a master lease agreement with GE Capital, their first step is to obtain a quote from GE Capital, whether they are purchasing or leasing equipment. After they have obtained that quote, different funding sources are analyzed to determine the best deal. If a funding source is cheaper than GE Capital, GOT submits a request to the Finance and Administration Cabinet for approval to use cheaper financing alternative. He said in most cases, the GE Capital Master Lease Agreement with the state is cheaper.

Mr. Thompson said GOT is moving to a desktop computer management model over the next three years in which all of their desktop units will be leased (not a lease-purchase). He said the state needs to start thinking of desktops as a utility, and budgeting for them in the operating budget. This will avoid the need for a large capital expenditure to refresh desktops.

Ms. Valicenti said for equipment purchases by the Executive Branch, any procurement costing over \$50,000 that does not fall within their architectural standards, or that is not listed on any kind of state contract, is reviewed by GOT. Ms. Valicenti said given the state's budgetary situation, almost every purchase request will go to the Finance Cabinet, and will come to GOT for concurrence or review. In the last year, GOT has instituted the Project Management Framework. Each of the cabinets and agencies is asked to present GOT with a project plan prior to any hardware or software purchase.

Mr. Thompson said GOT has formed a group, known as Enterprise Contracting, within the Office of Administrative Services to assist in getting the best deal possible for those items which all state agencies need, such as voice equipment and work stations. The group helps develop Requests for Proposals (RFP) for enterprise-type contracts.

Ms. Valicenti said they do not routinely review proposed purchases made by universities, but they will do so if asked.

In response to a question from Representative Damron, Mr. Hintze said the GE Capital Lease's interest rate is based on the current market rate.

Representative Damron asked why GOT is under the Governor's Office instead of the Finance Cabinet. Ms. Valicenti said the CIO position was established in 1998, and a

separate office was established in 2000. She said placing GOT within the Governor's Office is considered a "best practice" and is the trend within the public sector.

In response to another question by Representative Damron, Ms. Valicenti said the employees of GOT are merit employees.

Mr. Hintze added that elevating GOT to a separate status within the Governor's Office was in part to give the CIO status equal to a cabinet secretary. He said if the office had been subsumed by Finance, that would not be the case.

Senator Leeper thanked Ms. Valicenti and Mr. Thompson for their presentation. He then called on Mr. Hintze and Armond Russ, Commissioner of the Department for Facilities Management, to present the monthly Finance and Administration Cabinet project report.

Mr. Hintze first discussed an allocation of \$567,000 from the Emergency Repair, Maintenance and Replacement Fund to correct a humidity problem at the Western Kentucky Veterans' Center at Hanson (Hopkins County). Mr. Hintze explained that the allocation will be used to cover the cost of addressing the humidity problem and to supplant some previously authorized but unrealized federal funds. Mr. Hintze explained that the federal government will only reimburse 65% of the actual bids received rather than the estimated costs established during the budget process. The failure to readjust the project scope once the project was bid went unnoticed within the Finance Cabinet until recently. He said they have initiated steps with the Department of Military Affairs and the Department for Facilities Management to make sure this kind of situation is not repeated.

Mr. Hintze said General Leslie Beavers, Department of Military Affairs, plans to apply for additional federal funds to help address the humidity problem, and they believe that request will be approved. If additional federal funds are received, the Emergency Fund will be fully reimbursed. Mr. Hintze said they hope to recover two-thirds of the cost of the humidity remediation project.

Mr. Hintze said there is also a humidity problem with the new Eastern Kentucky Veterans' facility in Hazard; however, it is not as acute and is still being assessed. He said because of the nature of the facility – a different location in the state, different temperatures, and a two-story configuration instead of one, and because there are still funds in the authorized project account, they do not believe they will need Emergency Funds to address any potential problems at this site.

Commissioner Russ said they actually became aware of this problem last year, and have been working diligently because of the seriousness of this issue. He said it has been a very difficult problem to resolve. They have worked with the manufacturer, and have hired an HVAC consultant and an architectural consultant to look at the building

envelope. He said they now feel that there is a design error causing the problem and have asked their legal staff to determine if there is legal recourse to recover some of the funds due to this error. The same firm that designed the Western Kentucky center HVAC, also designed the Eastern Kentucky one.

Mr. Hintze next reported a \$290,000 scope increase for the Renovate/Relocate Thomson-Hood Veterans Center Special Care Unit project. He said the scope increase will be used to accept the low bid. The increase will be covered by \$188,500 in federal funds and \$101,500 in unbudgeted restricted funds.

Mr. Hintze reported that the Department of Fish and Wildlife Resources plans to increase the scope of its land acquisition pool by \$1 million. He said the funds used to increase the pool are from funds the Department has recovered through an agreement with the federal government. Under agreement with the federal government, these funds can only be used for land acquisition.

In response to a question from Representative Damron, Mr. Hintze said these dollars would be carried forward to the next biennium if they are not completely used this year.

In response to a question by Representative Damron, Mr. Hintze said the Fish and Wildlife Commission makes the final decision as to which properties are purchased.

Mr. Hintze next reported a \$2,971,320 federally funded project for the Department of Military Affairs to install a premanufactured metal building at Bluegrass Station in Lexington. The building will serve as an aircraft paint building.

Representative Damron made a motion to approve three projects submitted by the Finance and Administration Cabinet listed under New Business Item 7(B)2, (B)3, and (B)4 on the agenda. The motion was seconded by Senator Buford and passed unanimously by roll call vote.

Mr. Hintze reported that the Finance and Administration Cabinet plans to upgrade security at the Central Laboratory facility in Frankfort. Mr. Hintze said the focus of this upgrade is to meet federal standards in the wake of the Homeland Security Initiatives. He said previously they reported a federal bioterrorism grant that was received by the Cabinet for Health Services, and some of those grant funds are to be used for lab equipment and testing devices and some were to be used for the physical facility. Mr. Hintze said a portion of what was received and reported to the committee previously is part of the project they are reporting today. He said \$560,000 of that previously reported federal grant will be used for the central laboratory security upgrade. In addition, the General Assembly appropriated \$750,000 in the 2003 Session as a line item for facilities security upgrades. Mr. Hintze said originally it was contemplated as a line-item for

facilities security upgrades in multiple facilities, but now it is considered necessary to use it all on the Central Laboratory.

Mr. Hintze said they have approved \$120,000 of excess General Funds for the Kentucky State Police to upgrade its forensic laboratory; these funds remain from last year, and are to be directed on a one-time basis to this upgrade in order for the State Police to receive accreditation of their laboratory by national standards to a level they have not been previously certified. Mr. Hintze said the full scope of the project is \$1,430,000.

Mr. Hintze said the first priority of this project will be to strengthen access control of the exterior and the interior of the Laboratory building, and to make some laboratory specific improvements for Health Services and the Kentucky State Police. He said they are trying to meet federal and national accreditation standards and that has prompted this infusion of funds into the Central State Laboratory .

Mr. Russ added they will be constructing two mail-handling facilities, one at the exterior dock where mail and packages are received, and a second mail-handling facility in the Health Services lab.

Representative Damron made a motion to approve the project consolidation and scope increase. The motion was seconded by Senator Rhoads and passed by unanimously by roll call vote.

Mr. Russ reported a lease renewal report for the Governor's Office for Technology (PR-3947) in Franklin County. The property is owned by T & J Rentals (John Bohn and A.F. Manley.) The rate will increase from \$6.48 to \$8.70 per square foot and the annual cost of the lease is \$211,288.

Senator Rhoads made a motion to approve the lease renewal report. The motion was seconded by Representative Marcotte and passed unanimously by roll call vote.

Senator Leeper said the next agenda item was the bond activity report from the Office of Financial Management. He asked Mr. Warren Nash, Deputy Commissioner for the Department of Financial Incentives, Economic Development Cabinet, to report one new Economic Development Bond (EDB) project. Mr. Nash presented an EDB project to benefit Harman/Becker Automotive Systems, Inc., a manufacturer of car audio equipment. The Cabinet is proposing to make a grant of \$71,500 to Harman/Becker, through the City of Franklin in Simpson County. Proceeds will be used to help defray a portion of the cost associated with site preparation for the company's proposed 45,000 square foot expansion.

Senator Buford made a motion to approve the EDB grant. The motion was seconded by Representative Marcotte and passed unanimously by roll call vote.

Senator Leeper said there were three new Kentucky Infrastructure Authority (KIA) 2020 Account Fund B Grants: Columbia-Campbellsville – Waterline study interlinking two systems; City of Danville – Water treatment plant upgrade; and Jackson County Water Association – Construction of a lake or laying a transmission line to Rockcastle River. Senator Leeper said action was required for the Jackson County project, and the Committee conditionally approved the other project allocations in January 2002.

Senator Buford made a motion to approve a new KIA 2020 Account Fund B grant for the Jackson County Water Association contingent upon subsequent approval by the KIA Board. The motion was seconded by Senator Rhoads and passed unanimously by roll call vote.

Senator Leeper asked Mr. George Burgess, Executive Director, Office of Financial Management (OFM), and Mr. Tom Howard, Deputy Executive Director, OFM, to discuss the OFM report. Mr. Howard first presented five new bond issues: Kentucky Housing Corporation Housing Revenue Bonds, 2003 Series D & E or additional series as may be designated in an amount not to exceed \$80 million; University of Kentucky Consolidated Educational Buildings Revenue Bonds, Series S, dated July 1, 2003, \$29,655,000; University of Kentucky Housing and Dining System Revenue Bonds, Series S, \$52,830,000; State Property and Buildings Commission Revenue and Revenue Refunding Bonds, Project No. 77 in an amount not to exceed \$140,000,000; and Kentucky Economic Development Finance Authority Medical Center Revenue Refunding and Improvement Bonds, Series 2003A and 2003B (Ashland Hospital Corporation, d/b/a King's Daughters Medical Center project), \$29,425,000.

Representative Damron asked how the refunding bond issues will be structured. Mr. Howard said the bond issues will be structured so they are level over the remaining term of the original issues.

Representative Damron asked if OFM plans to issue a Tax and Revenue Anticipation Note (TRAN) this year. Mr. Howard said they are watching the market carefully. The current rate compression has had a dramatic negative impact on the ability to issue a TRAN effectively; currently, it costs less to borrow internally. He said they expect a change in the market in early July, which might prompt them to issue a TRAN.

In response to another question from Representative Damron, Mr. Hintze said the state had not budgeted any interest income from a TRAN.

Representative Damron made a motion to approve the five new bond issues listed under New Business Item 7D(3) on the agenda. The motion was seconded by Senator Buford and passed unanimously by roll call vote.

Senator Leeper said also included in members' folders were three follow-up reports (approval letters) for previously approved bond issues: Kentucky Housing Corporation Housing Revenue Bonds, 2003 Series B (AMT) and 2003 Series C (Non-AMT); Murray State University Housing and Dining System Revenue Bonds, Series P, dated June 1, 2003; and the University of Kentucky Hospital Refunding Revenue Bonds, Series A (Third Series), dated June 1, 2003. These bond issues were approved at an earlier committee meeting and did not require action.

Mr. Howard then reported 21 new bond issues with School Facilities Construction Commission (SFCC) debt service participation: Bell County, Berea Independent (Madison Co.), Breathitt County, Butler County (2), Clinton County, Elliott County, Estill County, Gallatin County, Jackson Independent (Breathitt Co.), Jefferson County, Letcher County, Lincoln County, Magoffin County, McCracken County, Oldham County, Owen County, Pulaski County, Rockcastle County, Taylor County, and Webster County.

Senator Leeper said the committee could not vote on these bond issues because the committee had lost its quorum.

Senator Leeper said there were four locally-funded school bond issues submitted to the committee for review this month: two for Fayette County and two for Jefferson County. He said all disclosure information has been filed, and no further action on the bond issues is required.

Mr. Hintze next discussed plans by the Kentucky Horse Park to allow private development on state-owned property. The United States Dressage Federation (USDF) will negotiate a long-term land lease with the Horse Park in order to build its headquarters within the National Horse Center Office Complex at the Horse Park. The office will be a 20,000 SF facility and will cost approximately \$3 million to build. The Horse Park expects the lease term to be 99 years at a nominal fee. At the end of the lease term, the Horse Park would own the property.

Mr. Hintze said the Thoroughbred Retirement Foundation (TRF) plans to build a facility adjacent to Horse Park property along I-75. The Foundation will lease 22 acres from the Horse Park for 15 years, and at the end of the lease term, the facility will belong to the Horse Park. The estimated cost for the facility is \$750,000.

Senator Leeper asked why the lease with the Horse Park Foundation is for only 15 years. Mr. John Nicholson, Executive Director, Kentucky Horse Park, said the TRF plans



to construct a very elegant barn and office complex, and the fact that it would revert to the Horse Park in 15 years appeared to be a good deal for the state. Mr. Nicholson said at the end of the lease term, the Commonwealth will lease this space back to TRF.

Senator Leeper noted the Horse Park Foundation has funded two other capital projects in recent years, the Walnut Ring and the Stadium Jumping Pavilion. Senator Leeper noted the Walnut Ring, an outdoor competition ring built at a cost of \$442,744, exceeded the \$400,000 threshold for a capital project, and as such, should have been submitted to the committee for review. He asked why this project was not submitted to the committee. Mr. Nicholson said they were very mindful that they needed to report all construction projects, but this particular project was completed prior to the committee's November 2002 directive relating to private development on state property. He said they intend to inform the committee of any construction or expansion at the Horse Park.

Mr. Hintze said it was a mistake, and it should have been reported. He said they believe any improvement of a capital nature of \$400,000 or more should be reported on a monthly basis. He said this project was not identified in the regular reporting process, and they will be more aware.

Senator Leeper said the committee's next two meetings are August 19 in Frankfort and September 16 at the Wendell H. Ford Training Center in Greenville.

With there being no further business, Representative Damron made a motion to adjourn the meeting. The motion was seconded by Representative Marcotte. The meeting adjourned at 2:15 p.m.